

The Army's Small Business Program: Contributing To A Healthy Economy

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Abstract. In the 1999 Economic Report of the President, President Clinton states that "Our nation is enjoying the longest peacetime economic expansion in its history." Small businesses account for 99.7 percent of the nation's employers, employ 53 percent of the private non-farm workforce, represent 47 percent of all sales in the country, and contribute a major share of the 3.1 million new jobs created. As the Army continues to downsize, its reliance on contractors to provide sustaining base supplies and services will continue to increase. In FY1998, the Army procured \$27B worth of supplies and services, of which, \$7.4M went to small businesses. The Army's support of small businesses is based on The Small Business Act of 1953. Small businesses play an important role in keeping the U.S. economy healthy by promoting efficiency and innovation, creating new jobs, allowing access to the American Dream, and contributing to the stability of the local community.

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Introduction

You have recently been assigned as the Project Manager for the construction of a new lodging facility to replace Knadle Hall at Fort Belvoir, VA. The new facility must be completed within six months because Knadle Hall has been condemned by the Department of Health and is scheduled for demolition within six months. Design plans are drawn and approved by the Commander. The construction of the new lodging facility will be contracted out since the Army does not have the in-house resources to build a new lodging facility. You have spoken to the Contracting Officer about the project and its urgency. You then hear those two words - small business. Aghh! How could this happen on my project and why does the Army support small businesses anyway? This paper will explore why the Army supports small businesses through its Small Business Program, and how the Army's support of small businesses contributes to a healthy economy.

Sustaining Base Support

The U.S. Government is the largest buyer of supplies and services in the world. During FY1998, the U.S. Government procured \$182 billion worth of supplies and services, of which, \$33 billion, or 18 percent went to small businesses (SBA, Federal Procurement, 1999). Of the \$182 billion, the Army accounted for \$26.5 billion, of which, \$7.4 billion, or 28 percent went to small businesses (DA, SADBUE, 1999). As the Army continues to downsize, its

reliance on contractors to provide sustaining base supplies and services will continue to increase. Purchases include construction of new lodging facilities, refuse collection, office supplies, and just about every category of supplies and services necessary to support our sustaining base (SBA, Practical Guide, 1999).

Why Small Business

A small business can be defined in many ways, from the average annual revenue by industry to the number of employees in the company. Generally, the Small Business Administration considers a business with less than 500 employees as a small business (SBA, The Facts About SB, 1999).

There are three primary reasons the Army supports small businesses. First of all, there is a long history of the Army purchasing its supplies and services from small businesses. As early as the Revolutionary War, through the Civil and World Wars, and continuing through today, sustaining base supplies and services have been purchased from small businesses (Blackford, 1991).

Secondly, it is the law. The Congress recognized the importance of small businesses to the U.S. economy and passed The Small Business Act in 1953 (Public Law 163, 83d Congress, 67 Stat. 239). The Small Business Act states that a fair proportion of the total Department of Defense purchases are to be placed with small businesses (SBA, A Practical Guide, 1999). This fair proportion is determined each year by the U.S. Small Business Administration and the Department of Defense. The Department of Defense, in turn, assigns separate small business goals to all of its Military Departments including the

Army. The Army's FY98 small business goal was that 27.9 percent of its total purchases should be placed with small businesses (DA, SADBUE, 1999).

Thirdly, and most importantly, support of small business makes good economic sense. In 1998, small businesses accounted for 99.7 percent of the nation's employers, employed 53 percent of the private non-farm workforce, represented 47 percent of all sales in the country (The House, 2000), and contributed a major share of the 3.1 million new jobs created (SBA, The Facts About SB, 1999). Small businesses are an important contributor to both the defense industrial base and the U.S. economy. Small businesses introduce innovation to the defense marketplace, and have been described as the "engine that provides job creation and ensures a greater number of citizens receive benefits from defense procurement dollars" (Cohen, 1999, p. 177).

U.S. Economy

In his 1999 Economic Report of the President, President Clinton states that "Our Nation is enjoying the longest peacetime economic expansion in its history...wages rising at twice the rate of inflation...and unemployment and inflation at their lowest levels in three decades" (Council, 1999, p. 3). In fact, as of December 1999, the unemployment rate is at a low 4.1 percent (BLS, 2000), the economy is growing at a robust 5.7 percent a year, and the inflation rate is at a low 1.7 percent (Commerce Dept., 2000). Small businesses contribute to this healthy economy by promoting economic efficiency and innovation, creating new jobs, allowing access to the American Dream, and contributing to the stability of the local community.

Economic Efficiency

One of the commonly held myths about small businesses centers on Adam Smith's economy of scale theory (Acs, et al., 1998). In his theory, Smith described a principle that he called the division of labor, which dramatically increases worker productivity and efficiency, and reduces the cost of goods sold. This division of labor involved the specialization of labor, with workers performing a single step instead of making the entire product. As workers become more efficient in performing their specialized functions, productivity increases and the cost of goods decreases (Hammer, et al., 1993).

In Smith's theory, small businesses do not play an important role in the U.S. economy because they are viewed as being less efficient than large businesses in producing a manufactured product. Their only role is to serve as suppliers to large businesses. Another theory, the economic efficiency theory, suggests that small businesses do play an important role in the U.S. economy.

Small businesses are actually more efficient than large businesses because small businesses focus on change. In the economic efficiency theory, small businesses do not enter the marketplace to increase the economic output and compete with large businesses. Small businesses enter the marketplace to serve as agents of change. Small businesses introduce change into the economy by creating new products and improving processes. These new products and processes represent a gain in the overall efficiency of the economy (Acs, et al., 1998).

In order to survive and compete in today's marketplace, small businesses operate more efficiently than large businesses. For example, as businesses continue to grow larger and larger, diseconomies of scale, such as bureaucratic proliferation, begin to appear. At the IBM Credit Corporation, a request for financing touches seven hands from the time a field salesperson makes the request. The steps involved include logging in the request, entering the data into the computer system, checking requester's credit, modifying the standard loan covenants, determining the interest rate, and preparing and sending the quote letter. Different people, in separate branches within the company, perform each step. This whole process takes six days on the average to complete. Diseconomies of scale make large businesses less efficient than small businesses (Hammer, et al., 1993).

Innovation

Businesses that innovate more consistently and rapidly are better able to compete in today's rapidly changing and highly competitive marketplace. These businesses require highly creative workers, pay higher salaries, and offer more job stability for their workforce. Small businesses play a critical role in the experimentation and innovation of new technologies, new products, and new services. Small businesses are more likely to respond and are quicker to bring to market new products or services because they are more market-driven and less research-driven than large businesses. (SB, Job Creation, and Growth, 1999).

Small businesses act as agents of change. Many innovative products and services usually come just a few years after a small business is founded (Acs, et al., 1998). Small businesses produce 55 percent of the innovations, obtain more patents per sales dollar, and make more discoveries than large businesses (SBA, The Facts About SB, 1999). The successful small businesses are those that develop some type of innovative activity, which offers consumers new products or services (Acs, et al., 1998). Among the important inventions by small businesses in the 20th century are the airplane, audio tape recorder, double-knit fabric, soft contact lenses, the zipper, and the personal computer (SBA, The Facts About SB, 1999).

Job Creation

In 1998, there were 24.8 million non-farm businesses in the U.S., of which, 99 percent were small businesses. Additionally, a record number of new small businesses, 898,000, were started that year (SBA, The Facts About SB, 1999). In terms of job creation, virtually all of the 11.2 million net new jobs added to the economy between 1992 to 1996 were generated by small businesses. As large businesses continue to downsize, with separations exceeding hires, small businesses are now responsible for creating most new jobs. During this period, small businesses created 11.8 million new jobs while large businesses lost a net 645 thousand jobs. Small businesses with 1 to 4 employees generated 52 percent of the net new jobs, and those with 5-19 employees created another 20.3 percent of net new jobs (SBA, SB Answer Card, 1999). Looking to the future, 71 percent of the new jobs in the nation's fastest growing industries,

health services and business services, will come from small businesses. By 2005, small businesses will contribute 5.2 million of the 7.2 million new jobs created in these fast-growing industries (House SB Committee, 2000).

The American Dream

Small businesses are the vehicles by which millions of men, women, minorities, and immigrants access the American Dream. The greatest source of America's strength has always been in the American Dream of economic prosperity, equal opportunity, and upward mobility (Acs, et al., 1998). From the founding of the first colonies to the present day, small businesses have played an integral part in the development of the economic and social fiber of this nation. Throughout the world, people associate the small business owner, as epitomizing all that is good about the American way of life (Blackford, 1991).

The U.S. Government supports policies that facilitate the American Dream by eliminating barriers to entry, unfair methods of competition, and restraint of trade (Acs, et al., 1998). Congress has assisted facilitating the American Dream with the passage of the Federal Trade Commission Act and the Clayton Act in 1914, and the Small Business Act in 1953. The Federal Trade Commission Act established the Federal Trade Commission to look at unfair methods of competition, while the Clayton Act condemned the restraint of trade (Blackford, 1991).

Local Community

Finally, small businesses contribute to the vitality and stability of the local communities where they are located. A small business with 100 employees in

a town adds 351 more people, 97 more families, 79 more school children, \$490K more bank deposits, one more retail establishment, \$565K more retail sales per year, and \$1,036K more personal income per year. Small businesses also support their local communities by giving more goodwill per employee to community service organizations than do large businesses (House SB Committee, 2000).

Conclusion

The Army has a long and proud tradition of contracting with small businesses to provide sustaining base supplies and services and will continue to do so in the future. The Army exceeded its FY1999 small business goal of 26.0 percent by awarding 27.4 percent of its contracts to small businesses (Sarah Cross, telephone communication, February 28, 2000). The Army, the U.S. economy, and the local community benefit from the Army's contracts with small businesses.

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